In the Matter of the Nebraska Public Service Commission, on its own motion, seeking to establish a long term universal service funding mechanism	)))))	Application No. NUSF-26 Progression Order No. 4

Comments of Citizens Telecommunications Company of Nebraska, d/b/a Frontier Communications of Nebraska

Citizens Telecommunications Company of Nebraska, d/b/a Frontier Communications of Nebraska ("Frontier") hereby submits comments in the above-referenced docket entered by the Nebraska Public Service Commission ("Commission") on January 7, 2003 ("January 7th Order"). Frontier appreciates the opportunity to supply input into the development of the long-term universal service funding mechanism and is generally supportive of the Commission's decision to select a density-based model to calculate Nebraska's universal service funding. Frontier has identified the following issues and provides recommendations for the Commission to consider and address as it progresses with this proceeding:

1.) There is some inconsistency between use of households to determine costs and apportionment of funding on the basis of access lines. However, absent other commenters offering a reasonable alternative, the proposed methodology provides a reasonable balance of administrative ease and accuracy.

2.) Out-of-town households are being disproportionately allocated to less-populated exchanges. Frontier recommends a one-time adjustment be made to correct the apparent over-apportionment of households in areas where the ratio of access lines to total households by exchange is less than .94.

3.) The Commission seeks comments on whether the Hatfield model includes costs which are not related to basic local service. Frontier believes the Hatfield model's USF module includes only costs related to supported basic local services. Further, Frontier recommends that the Nebraska state USF support only residential lines.

4.) An adjustment to funding levels for differences in network quality would be highly subjective, vary for a given provider from area to area, and perhaps result in bias from one type of provider to another. Frontier recommends no attempts be made to adjust for differences in networks. The market will "self-police" service quality.

5.) It is unclear to Frontier whether the Commission intends to use a company-specific or statewide revenue benchmark. Frontier recommends use of a statewide revenue benchmark.

6.) An earnings test based on embedded costs: is inconsistent with use of a forward-looking proxy model; fails to offer incentives for efficiency; is inconsistent with a truly portable funding mechanism; and would require competitors with differing levels of regulation and accounting regulations to be monitored on a uniform basis. Frontier recommends the funding be based on the forward-looking cost methodology outlined by the Commission without the introduction of an embedded cost adjustment.

Cost vs. Support Application and Apportionment

The Commission proposes to develop costs based on density using the Hatfield model version 5.0a with adjustments. The January 7th Order states "density" will be based on households, using town and county 2000 census data divided by square miles[1]. Appendices A and B to the Commission's January 7th Order identify the calculated "town" and "out-of-town" densities using the proposed methodology. The Hatfield model will be then populated with the calculated density based on households, rather than the Hatfield model's density of total lines divided by total area[2].

The "revenue benchmark" is proposed to be the tariffed local rate, including any zone charges, and the tariffed subscriber line charge[3]. The level of support within each support area will be determined by the difference between the cost supplied by the Hatfield model (cost per household) and the revenue benchmark (revenue per access line) [4]. Each company's support will be based on the ratio of lines that the company served compared to the total lines in a support area[5]. Frontier believes there is an inconsistency with the cost being based on households and the application and apportionment of the support being

[1] See Nebraska Public Service Commission's Application No. NUSF-26, Progression Order No. 4, entered January 7, 2003, at para. 19.
[2] See Id. at para. 21.
[3] See Id. at para. 25.
[4] See Id. at para. 26.
[5] See Id. at para. 30.

based on access lines. However, as long as households in out-of-town areas are adjusted, as recommended later in comments, Frontier believes this methodology may be the best alternative considering the apparent lack of other viable options and the need for a method that can be reasonably administered.

Distribution of Out-of-Town Households

The Commission seeks comments on whether it would be appropriate to assume that households outside of towns are evenly distributed within the out-of-town areas[6]. While it is convenient and might seem reasonable to assume households are evenly distributed, a review of data for Frontier exchanges suggests households are not evenly distributed resulting in inaccurate levels of density in out-of-town areas. Further, the review suggests that use of this assumption especially skews results for the smaller exchanges – those areas where accurate data is most important for purposes of determining USF support levels.

The average telephone penetration rate for Nebraska is .94 residential access lines per household, based on the Telephone Penetration by State Report published by the FCC[7]. For purposes of validating the number of households assigned under the average distribution methodology, Frontier compared its residential penetration rate based on the Commission's proposed even distribution of households methodology to the statewide average

[6] See Id, at para. 20.

penetration rate. Based on an assumed threshold of the statewide average of 94 access lines per 100 households, the Commission's proposed even household distribution methodology overstated households in 22 of Frontier's 37 exchanges. Please see attached Exhibit 1. In other words, the access line penetration rate for those 22 exchanges was lower than .94. This overstatement of the level of households and understatement of access line penetration would undoubtedly be even greater if the multiple access lines within households were excluded from this analysis. Interestingly, it was Frontier's smaller exchanges that had the highest frequency of overstated households. One of Frontier's smaller exchange areas, Miller, with a population of 156, has a calculated penetration rate of only .35. Conversely, Frontier's largest exchanges, including Kearney and Columbus, appear to have lower apportioned households than expected, with access lines per household of 1.30 and 1.26, respectively.

Frontier recognizes that it is impractical to assign households to out-of-town areas of exchanges with absolute precision, but suggests that an adjustment be employed to correct for overstatement of households in out-of-town rural areas. Specifically, Frontier recommends that a "household cap" of 1 household per .94 access lines be employed to recalibrate the initial household counts for rural areas.

[7] See http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/trend502.pdf , Table 17.2, page 134 of 173.

Hatfield Model

The Commission seeks comment on whether the Hatfield model results include costs not attributable to the provision of basic local exchange service[8]. The Hatfield model, HAI Model Release 5.0a, was developed to provide cost detail for unbundled elements used to provide basic local exchange service. Specifically, the costs included per the HAI Model are: the loop, the switch line port, the local minute portions of end office and tandem switching, transport facilities for local traffic and the local portions of signaling costs. The model also includes costs associated with retail uncollectibles, variable overheads, and certain other expenses required for basic local service, such as billing and bill inquiry, directory listings and number portability.[9] The model user has the ability to select the portions of non-traffic-sensitive UNEs to be included in the supported basic local service.

The Density Zone USF sheet of the Hatfield model contains separate state and federal fund calculations. The user can select separate state and federal cost benchmarks, and separately specify the particular services (e.g., primary and secondary residential lines, single line business, etc.) to be supported.[10]

Frontier recommends that Nebraska universal service funding should only be calculated and provided for residential lines. This is consistent with the Commission's decision to use "households" in calculating the costs for providing service since "households" would correlate to residential lines and not business

[8] See NUSF-26, Progression Order No. 4, at para. 23.
[9] HAI Model Release 5.0a, Model Description, HAI Consulting, Inc., February 2, 1998, Section 6.6.4.2
[10] Ibid

lines. If inflation and household growth rates are being used as capping mechanisms, then the line counts within each support area must be reported households, or residential lines, if households per the Census include any single line business establishments.

Cost Adjustments For Telecommunications Network Differences

The Commission is asking for comment on whether costs should be adjusted to reflect differences in costs between companies and the quality of the telecommunications network in place[11]. Frontier recommends no adjustment be made for costs and quality differences between companies since such an adjustment would be subjective and require continual modifications over time as changes are made to the network or quality of service. Making an adjustment would result in inconsistent funding among providers within an area or one provider's funding based on the quality or network changes made by other providers. In addition, even within one telephone company's network, the quality and costs of facilities may vary greatly by area or exchange. The Commission would have difficulties in determining how to make adjustment to account for these intra-company differences. Lastly, the market will "self-police" service quality; i.e. sub-standard service will result in lowering market share and, ultimately, lowering the level of support.

Setting the "Revenue Benchmark"

[11] See Id, at para. 24.

The Commission proposes that cost less the revenue benchmark will determine the support amount per household. The "revenue benchmark" is calculated as the tariffed local rate, including any zone charges, and the tariffed subscriber line charges[12]. Frontier is unclear from the January 7th order whether the Commission intends to apply a statewide revenue benchmark for all carriers using averaged tariffed local rates and subscriber line charges or whether the Commission anticipates each company having a different revenue benchmark. Frontier recommends that the revenue benchmark should be a fixed, statewide benchmark that is the same for all carriers. Without a statewide benchmark, there would be incentives to reduce tariffed rates to garner market share without the consequence of lowering revenue, since USF support would make up the difference. Also, wireless providers do not file tariffs and do not have subscriber line charges as do local exchange carriers. A uniform benchmark is essential for competitive parity.

Earnings Test

The Commission states that the final provision of NUSF support will be subject to an earnings test. Companies whose earnings exceed the Commission's established benchmark of 12% will have their NUSF support reduced by an amount equal to the amount of the earnings above the Commission revenue benchmark[13]. It is not consistent to introduce an earnings benchmark that is calculated using an embedded cost methodology into the state

[12] See Id, at para. 25.
[13] See Id, at para. 31.

USF model which is calculated using forward-looking costs. It would not be appropriate to reduce funding to an efficient low cost provider while rewarding an inefficient higher cost competitor with funding.

Moreover, it is not clear how the earnings test would be applied in areas where two or more telecommunications providers are competing and offering service. To minimize the opportunity for competitive arbitrage, funding should be based on the same assumptions for two carriers competing in the same area. It would not be appropriate to deny one provider funding support based on the earnings of a competitor. Introducing an earnings adjustment into this calculation would also require wireless and other CLECs to provide earnings information under a uniform accounting mechanism. Wireless providers are not subject to USOA accounting rules and CLECs are very loosely regulated for purposes of telecommunications regulation accounting. Finally, there is a potential for abuse or unintended consequences when comparing earnings of different types of companies (ILECs, CLECs and wireless providers) into what should be a uniform earnings review.

Corrections needed to Appendix A of NUSF-26, Progression No. 4

Frontier notes that specific cities listed as “Citizens” in Appendix A are actually Qwest properties. These cites are as follows: Atkinson, Atlanta, Creston, Emerson, Emmet, Farwell, Howells, Humphrey, O’Neill, Oxford, Pilger, Randolph, and Silver Creek.

Respectfully submitted this 7th day of March, 2003,

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